



House of Commons  
Public Accounts Committee

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# Central government's management of service contracts

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Seventeenth Report of Session  
2008–09

*Report, together with formal minutes, oral and  
written evidence*

*Ordered by the House of Commons  
to be printed 23 March 2009*

## The Public Accounts Committee

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### Committee staff

The current staff of the Committee is Mark Etherton (Clerk), Lorna Horton (Senior Committee Assistant), Pam Morris (Committee Assistant), Jane Lauder (Committee Assistant) and Alex Paterson (Media Officer).

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## Summary

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In 2007–08, central government spent over £12 billion on service contracts, primarily in the areas of information and communication technology, facilities management and business process outsourcing, and an estimated £240 million on managing these contracts.

In most cases central government monitors the performance of its suppliers, but it makes limited use of financial incentives to encourage suppliers to improve performance. In addition, 38% of contract managers did not always apply financial penalties where suppliers under-performed. The extent to which central government tests the value for money of ongoing services and contract changes is variable. For example, 41% of contract managers had not tested the value for money of new services purchased under an existing contract.

Planning and governance is one of the weaker areas of contract management, although there are examples of good senior level engagement. Less than half the organisations surveyed, however, had an individual with overall responsibility for contract management, and there was no documented plan for managing 28% of contracts. In addition, many contracts do not have in place some or all of the elements of good practice risk management; for example, 56% of contracts did not have a contingency plan in case of supplier failure and 30% of contracts where suppliers were dealing with personal or security information did not have a risk register.

No commercial director/head of procurement rated the level of resources allocated to the management of their major contracts as ‘good’, and 22% of contract managers considered they did not have time to perform their responsibilities well. Most contract managers had undertaken relevant training, although 60% of organisations did not provide a structured training programme for their staff.

The Office of Government Commerce is to issue further guidance on contract management in April 2009, building on the good practice framework it published jointly with the National Audit Office, and it is working to improve the provision of training on contract management. It is also extending its monitoring of major suppliers to government, and is reviewing recent examples of service failure where contractors failed to perform—involving SATS tests and Educational Maintenance Allowances—to identify lessons for the future.

On the basis of a report by the Comptroller and Auditor General,<sup>1</sup> we examined how well central government is managing service contracts and the effectiveness of the Office of Government Commerce in supporting central government to improve contract management.

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1 C&AG's Report, *Central government's management of service contracts*, HC (2008–09) 65



## Conclusions and recommendations

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- 1. Achieving value for money depends on effective contract management but central government does not accord contract management sufficient attention.** The emphasis continues to be on the early stages of letting of a contract rather than on managing it afterwards. To help achieve a better balance, central government organisations should assign responsibility for contract management policy, practice and capability to a single individual, whose responsibilities should include ensuring that all major service contracts have appropriate governance arrangements and documented contract management plans.
- 2. Not all major service contracts include performance measures to manage the performance of suppliers.** Without such measures, central government cannot effectively measure and drive supplier performance. Central government organisations should ensure that all their major service contracts have performance measures, and that these measures are updated as necessary to meet changing business requirements.
- 3. The failure to enforce financial penalties whenever suppliers under-perform increases the risk that relationships between central government and suppliers are too cosy.** Central government organisations should apply financial penalties when contracts entitle them to do so unless there are very exceptional circumstances why they should not. The Office of Government Commerce should develop guidance to set out what these exceptional circumstances are, with a view to minimising the loss to the taxpayer.
- 4. Central government organisations do not routinely test the value for money of their service contracts.** As a result, there is no assurance that the contracts concerned are providing value for money and that opportunities for savings are not being missed. The expectation should be that the value for money of ongoing services provided under major service contracts should be tested at least every three years. All significant changes to major service contracts should be tested as a matter of course.
- 5. No central government organisation rated the level of resources devoted to managing their major service contracts as 'good'.** As a result, opportunities for securing better value for money may be missed and risk may not be managed effectively. Central government organisations should undertake a review of the resourcing of contract management activities across their portfolio of major service contracts and take action where the review indicates that resources are not being used to best effect.
- 6. Central government organisations are not providing adequate support to their contract managers.** Organisations should improve the support available by providing contract management training where necessary to supplement the arrangements being put in place by the Office of Government Commerce and by establishing contract management communities to facilitate the sharing of best practice among contract managers.

7. **Risk management arrangements are inadequate for many contracts.** Despite involving the delivery of critically important services, over half of contracts did not have a contingency plan in case of supplier failure. And even 30% of contracts where suppliers were dealing with personal or security information did not have a risk register. Central government organisations should review the risks associated with their major service contracts and put in place good practice risk management processes, including risk registers and contingency plans.
8. **The Office of Government Commerce has not previously provided sufficient contract management guidance or monitoring of major suppliers.** During 2009, it plans to issue further guidance and develop new training on contract management, and extend its monitoring of the major suppliers to government. These are important initiatives which should help central government secure better value for money from its service contracts, and the Office of Government Commerce must deliver on its plans. The National Audit Office estimated that between £160 million and £290 million a year could be saved through better contract management.
9. **The recent problems with SATS tests and Educational Maintenance Allowances have demonstrated that service failure by contractors can have a major impact on citizens.** The outsourcing of services means central government's role becomes one of contract management, and every effort needs to be made to avoid similar difficulties arising on future contracts. The Office of Government Commerce should publish the lessons from the reviews it is carrying out into these two cases, including particular lessons on contract management.

# 1 Managing suppliers to secure value for money

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1. Contract management is especially important where suppliers are engaged to provide services over a long period of time—for 10 years or more on occasion—and customers need to ensure that service levels and value for money are maintained over the duration of the contract. Having performance measures and keeping them up-to-date is essential for managing supplier performance. In most cases, central government regularly collects performance information and discusses performance with suppliers, though key performance indicators are not always updated to keep pace with changing business requirements. An exception at the time of the National Audit Office's work was the Foreign and Commonwealth Office, which had no formal performance measures for managing its contract for travel services, worth £23 million a year, although the contract had been in place since December 2007.<sup>2</sup>

2. Good contract management should also include financial incentives to encourage suppliers to improve performance, and 80% of the suppliers surveyed confirmed that incentives did encourage them to perform. Central government makes limited use of financial incentives, however, with over a third of the contracts covered by the National Audit Office's survey having no provision for such incentives. Furthermore 38% of contract managers did not always invoke payment deductions where suppliers underperformed, even where the contract entitled them to do so.<sup>3</sup>

3. The Office of Government Commerce did not consider it surprising that contract managers did not always apply financial penalties. In its view, this finding did not indicate that relationships with suppliers were too cosy since there were situations where customers and suppliers were working closely together to improve performance and applying penalties would not be helpful. Nevertheless, the Office of Government Commerce accepted that there would also have been instances where penalties had not been applied but should have been. To secure value for money, relationships should be challenging, contracts should contain provision for financial incentives and penalties, and customers should not set penalties aside simply to avoid upsetting their suppliers.<sup>4</sup>

4. Where contracts run for a long time, the value for money of ongoing services and of major changes to the contract should be assessed regularly, for example, through price benchmarking or market testing. Doing this can result in significant savings. The Home Office, for example, saved £17 million a year on its IT contract by benchmarking the service against market prices. Of the contract managers surveyed, however, 25% of those responsible for contracts that had been running for at least three years had undertaken no value for money testing of ongoing services. And 41% of contract managers had not tested the value for money of new services.<sup>5</sup>

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2 Qq 25–27; C&AG's Report, paras 1.6, 2.14–2.16

3 C&AG's Report, para 2.19

4 Qq 10–12, 64–65, 90

5 C&AG's Report, paras 2.25–2.28

5. The Office of Government Commerce confirmed that periodic value for money testing, particularly where there are changes to a contract, is an important requisite of managing complex contracts. While the very large contracts usually did provide for benchmarking or other kinds of value for money testing, many contracts did not. The Office of Government Commerce would therefore stress in its guidance the importance of building regular opportunities to test value for money into future contracts.<sup>6</sup>

## 2 Governance, resourcing and risk management

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6. Planning and governance was one of the weaker areas in the contracts assessed by the National Audit Office, with six of the eight contracts rated as amber or worse, a finding consistent with the results of the Office of Government Commerce's own Procurement Capability Reviews. The National Audit Office also found, however, examples of excellent senior level engagement, for example, by the Permanent Secretary at the Department for Work and Pensions, who is actively involved in the management of major suppliers. In the Office of Government Commerce's view, Permanent Secretaries increasingly understood the importance of getting contract management right and of having proper governance, and most were personally involved in some aspects of procurement and in commercial matters more generally in their departments.<sup>7</sup>

7. It is also helpful for there to be a single point within a department for contract management policy, practice and capability, although fewer than half the organisations (43%) surveyed by the National Audit Office had an individual with overall responsibility for contract management across the organisation. In addition, there was no documented plan for managing 28% of contracts. The Office of Government Commerce considers that it should be standard to have a documented plan for managing major contracts and it would make this clearer in future guidance.<sup>8</sup>

8. In 2007–08, central government spent the equivalent of 2% of annual contract expenditure (an estimated £240 million) on managing service contracts. Having sufficient people with the right experience and skills is essential to effective contract management, but no commercial director/head of procurement rated the level of resources allocated to the management of their major service contracts as 'good'. In addition, 22% of the contract managers surveyed considered they did not have time to perform their responsibilities well. Resources were stretched, for example, at the Ministry of Justice, where the manager of the contract for court security, worth £29 million a year, also managed two other major contracts.<sup>9</sup>

9. The Office of Government Commerce does not consider it is possible to specify what percentage of the contract value should be spent on contract management as this will depend on the level of risk, the value for money opportunities, and the importance of the contract to the organisation. It would, however, review whether it could provide more advice on resourcing as part of future guidance on contract management.<sup>10</sup>

10. Over three-quarters of the contract managers surveyed had three or more years experience of managing major contracts, with 14% having one year's experience or less. Most contract managers had no formal commercial qualification but had undertaken some

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7 Qq 21, 33–36; C&AG's Report, para 2.3; Figure 9

8 Qq 15–16, 54; C&AG's Report, paras 2.4–2.5

9 C&AG's Report, paras 2.6–2.8

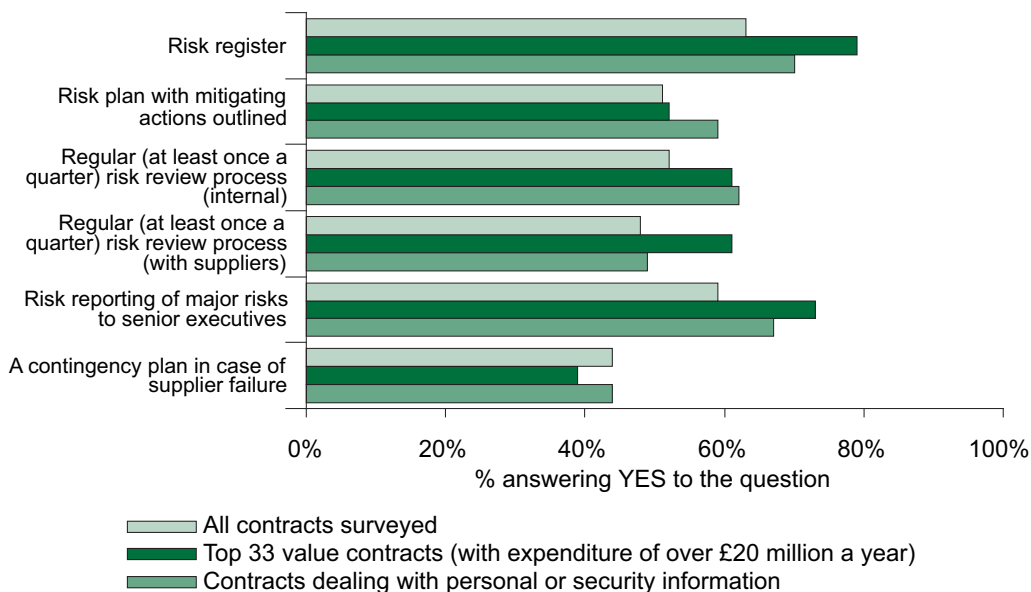
10 Qq 55–58

relevant training, although 60% of organisations did not provide a structured training programme for their staff. There was also a lack of established contract management ‘communities’ where contract managers could discuss issues and share good practice.<sup>11</sup>

11. The Office of Government Commerce considers that ensuring that contract managers receive the right training and development, and that they are part of a community so they can exchange best practice, is more important than professional qualifications. The Office of Government Commerce is taking action to bring contract managers into the fold of the procurement profession, which in the past has often not been seen as including contract managers. It is identifying contract managers across government, and at the time of our hearing Permanent Secretaries had just approved plans for career development, talent management, and learning and development across the government procurement profession, together with a reward strategy.<sup>12</sup>

12. Most service contracts are critical to the delivery of an organisation’s business objectives and carry significant risk if the supplier fails. Despite this, many of the contracts in the National Audit Office’s survey did not have in place some or all elements of good practice risk management (**Figure 1**). For example, 37% did not have a risk register and 56% did not have a contingency plan in case of supplier failure. The Office of Government Commerce accepts that there is more to be done on risk management, particularly given the prevailing economic circumstances. Though guidance is available, risk management is not embedded in all contracts.<sup>13</sup>

**Figure 1: Risk management processes in place across central government service contracts**



Source: Comptroller and Auditor General's Report, Figure 13

11 C&AG's Report, para 2.10

12 Qq 8–9, 38–39

13 Qq 2–4; C&AG's Report, paras 1.5, 2.21; Figure 13

13. Two-thirds of the contracts in the National Audit Office's survey involved suppliers dealing with personal or security information, but even 30% of these contracts did not have a risk register. The Driving Standards Agency, for example, did not have a specific risk register for its contract for driving theory tests prior to the supplier losing a computer hard disk drive containing personal information about test applicants. The Office of Government Commerce pointed to the amount of work that was underway across government on data security. The Government had made clear to its largest suppliers their obligations in respect of handling sensitive and personal data, and there would be mandatory security clauses in future contracts to that effect. For example, suppliers' staff should be trained in areas such as the secure transfer and disposal of data.<sup>14</sup>

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14 Q 23; C&AG's Report, paras 2.21–2.23; Ev 12

### 3 The effectiveness of the Office of Government Commerce in improving contract management

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14. Although responsibility for managing contracts rests with the organisations concerned, the Office of Government Commerce plays a role in supporting central government to improve contract management, and during 2007 it carried out reviews to assess the procurement capability of 16 government departments. At the time of our hearing, ten of these Procurement Capability Reviews had been published, with the remaining six due for publication by April 2009. Among the themes emerging from the Reviews has been the need for better risk management and supplier relationship management, and overall there is considerable scope for departments to improve their contract management.<sup>15</sup>

15. Each department has an action plan for responding to its Procurement Capability Review and the Office of Government Commerce will check after three, six and twelve months to assess what progress departments have made. The Office of Government Commerce is satisfied that it has sufficient ability to influence central government effectively. It deals directly with Permanent Secretaries when issues arise, and Permanent Secretaries respond positively to take action where the Office of Government Commerce recommends it.<sup>16</sup>

16. The Office of Government Commerce provides contract management guidance, although this is fairly high level, and the key document was published seven years ago in 2002. Alongside the Comptroller and Auditor General's report, the National Audit Office and the Office of Government Commerce jointly published a good practice framework on contract management, on which the Office of Government Commerce will be building in further guidance to be published in April 2009.<sup>17</sup>

17. The Office of Government Commerce also has a role in making sure that appropriate learning and development is available, working with the National School of Government, the Chartered Institute of Purchasing and Supply and private sector training providers. The provision of specialist contract management training has been identified as a priority area, and the Office of Government Commerce is currently piloting training with the Department for Children, Schools and Families and is drawing on the best practice highlighted in the C&AG's report. Permanent Secretaries had also agreed that in future procurement professionals across government would be required to undertake 50 hours of professional development.<sup>18</sup>

18. The Office of Government Commerce works to improve the management of key suppliers to government through greater collaboration and intelligence sharing. To date, however, this work has not extended in any systematic way beyond suppliers of

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15 Q 7; C&AG's Report, paras 3.1–3.2

16 Qq 5–7, 93–94

17 Qq 15–17; C&AG's Report, para 3.5

18 Qq 50–52; C&AG's Report, paras 3.6–3.7

information and communication technology equipment. For this sector, the Office of Government Commerce has introduced a 'common assessment framework' for the top 15 suppliers, which are assessed every six months against 12 indicators including performance and value for money. The results are disseminated to departmental Chief Information Officers and performance improvement plans are developed for each supplier. The Office of Government Commerce is now expanding the common assessment framework approach to suppliers of IT software, and has also set up six other categories for collaborative procurement, such as energy, food and construction, where it will assess major suppliers to government.<sup>19</sup>

19. We asked the Office of Government Commerce about recent examples of high profile service failure where contractors had not performed, including the delays in the marking of SATS tests and in the payment of Educational Maintenance Allowances. While the appointment of particular suppliers is a matter for individual departments, the Office of Government Commerce is reviewing both these recent cases to identify what lessons can be learned for the future. Key questions for the Educational Maintenance Allowances review would be how the supplier was managed, whether government found out about the problems early enough, and whether it took appropriate action when the problems did become clear.<sup>20</sup>

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19 Qq 63, 68–69; C&AG's Report, paras 3.10–3.12

20 Qq 79–89

# Formal Minutes

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**Monday 23 March 2009**

Members present:

Mr Edward Leigh, in the Chair

Mr Richard Bacon  
Rt Hon David Curry  
Mr Ian Davidson  
Mr Nigel Griffiths

Rt Hon Keith Hill  
Mr Austin Mitchell  
Rt Hon Don Touhig  
Rt Hon Alan Williams

Draft Report (*Central government's management of service contracts*), proposed by the Chairman, brought up and read.

*Ordered*, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 19 read and agreed to.

Conclusions and recommendations read and agreed to.

Summary read and agreed to.

*Resolved*, That the Report be the Seventeenth Report of the Committee to the House.

*Ordered*, That the Chairman make the Report to the House.

*Ordered*, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

[Adjourned till Monday 30 March at 4.30 pm]

## Witnesses

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**Wednesday 14 January 2009**

*Page*

**Mr Nigel Smith, Chief Executive, Office of Government Commerce**

**Ev 1**

## List of written evidence

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1 Office of Government Commerce

Ev 12

2 Chelgate Limited

Ev 16

## List of Reports from the Committee of Public Accounts 2008–09

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First Report	Defence Information Infrastructure	HC 100
Second Report	The National Programme for IT in the NHS: Progress since 2006	HC 153
Third Report	Skills for Life: Progress in Improving Adult Literacy and Numeracy	HC 154
Fourth Report	Widening participation in higher education	HC 226
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Ninth Report	Protecting the public: the work of the Parole Board	HC 251
Tenth Report	New Dimension—Enhancing the Fire and Rescue Services' capacity to respond to terrorist and other large-scale incidents	HC 249
Eleventh Report	The United Kingdom's Future Nuclear Deterrent Capability	HC 250
Twelfth Report	Selection of the new Comptroller and Auditor General	HC 256
Thirteenth Report	Department for Work and Pensions: Handling Customer Complaints	HC 312
Fourteenth Report	HM Revenue and Customs: Tax Credits and Income Tax	HC 311
Fifteenth Report	Independent Police Complaints Commission	HC 335
Sixteenth Report	Department for International Development: Operating in insecure environments	HC 334
Seventeenth Report	Central government's management of service contracts	HC 152

# Oral evidence

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## Taken before the Committee of Public Accounts

on Wednesday 14 January 2009

### Members present:

Mr Edward Leigh, in the Chair

Mr Richard Bacon  
Mr Ian Davidson

Nigel Griffiths  
Mr Austin Mitchell

Mr Tim Burr, Comptroller and Auditor General, Mr Michael Whitehouse, Assistant Auditor General and Ms Laura Brackwell, Director, National Audit Office, gave evidence.

Ms Paula Diggle, Treasury Officer of Accounts, HM Treasury, gave evidence.

### REPORT BY THE COMPTROLLER AND AUDITOR GENERAL

#### CENTRAL GOVERNMENT'S MANAGEMENT OF SERVICE CONTRACTS (HC 65)

*Witness:* Mr Nigel Smith, Chief Executive, Office of Government Commerce, gave evidence.

**Q1 Chairman:** Good afternoon. Welcome back to the Committee of Public Accounts. We hope you all had a good rest. We welcome our witness, Nigel Smith, who is Chief Executive of the Office of Government Commerce. I am always pleased to see permanent secretaries flying solo, it shows self-confidence. Today we are considering the Comptroller and Auditor General's Report on *Central Government's Management of Service Contracts*, which I know does not sound terribly sexy to many politicians but I am sure you would agree it is very important, Mr Smith. After all, the Government spent over £12 billion on service contracts primarily in areas of information and communication technology in the last year, so when we are talking a lot about efficiency savings, as we are nowadays, this is a very, very important area. Can I just ask you a general question, Mr Smith, which is not particularly related to a paragraph in the report. Obviously we are living in difficult economic times and there have been a number of very high profile contractor failures in recent years. Have you evaluated the risk of widespread contractor failure?

**Mr Smith:** Yes.

**Q2 Chairman:** What does that evaluation tell you?

**Mr Smith:** At the moment it is more a feeling. I have got some work on at the moment having a look at the risks that do exist because you cannot ignore the fact that company viability is going to be under pressure. We have got some very large companies and some very small companies providing critical services into Government, so if we have got viability issues we have got to look more closely at what we do in terms of contingency planning, and that is referenced in the Report. In all of the Report that is the one area that I think I am most concerned about at the moment.

**Q3 Chairman:** We are here really, Mr Smith, not to have a go at you because you are on our side in all this, we are here literally to help you. I know we would say that, but permanent secretaries do not always believe it. In a sense, you are not running any of these contracts, you are here as a central Government enforcer of efficiency, so please feel free to answer our questions as fully and openly as you like because the more you say, the better the report we can do and we can help you in your work. For instance, I was rather worried looking at figure 13, which we can find on page 23, if you would like to look at that. This precisely relates to what you have just said, which was why I asked really. If you look at that last line: "A contingency plan in case of supplier failure", you will see that half of the contracts covered in the NAO's survey do not have contingency plans in case of supplier failure. These are presumably delivering critical services. Is this not rather worrying to you?

**Mr Smith:** As I said right at the start, the one issue in this Report which I think is where there is much more work to be done is on risk management, particularly given the economic circumstance. I should say that it is not for the want of guidance.

**Q4 Chairman:** From you?

**Mr Smith:** There is a lot of guidance, not just from OGC but from other quarters as well. For example, there is a module within the CIPS training specifically on risk management. It is perhaps ironic that people often do not understand that we produce some of the world leading advice on procurement policy, stuff that is used all around the world. We have a thing called MoR, which is the Management of Risk, which is one of the key management qualifications on risk management which is used in the States, all over the world. The issue is actually getting it embedded in all of the contracts.

14 January 2009 Mr Nigel Smith

**Q5 Chairman:** Why not? Do you not have the clout in central Government? Do you summon these permanent secretaries in, do you have a row with them? What happens? How does it work?

**Mr Smith:** I do not know whether I have a row with them, but I certainly do speak to the permanent secretaries.

**Q6 Chairman:** So what do they say when you point to a figure like I have just referred to and specifically raise their own department?

**Mr Smith:** They say to me, "We will do something about it".

**Q7 Chairman:** And do they?

**Mr Smith:** They do. The evidence of that is the Procurement Capability Reviews which really came out of *Transforming Government Procurement*. This sort of mirrors the Departmental Capability Reviews but, to be frank, I think it is much more granular. We have now completed and published ten of them. We have actually completed all of the reviews of all 16 central Government departments. We have not published them all yet, but we will do by April of this year. There are about eight issues that come out on a consistent basis. One of them is the risk management process and another one is the strategic relationship of the Supplier Relationship Management process, absolutely intertwined. This is all in the public domain because we took the decision early on to publish the results of our PCRs, we published the action plans and if you go on to our website I think you will see that six or seven out of ten have got risk management process as part of their action plan for their performance improvement. Yes, I have that conversation with permanent secretaries. I have it not just when it is done but after three months, after six months and I have just started to do the first 12 month stock takes to see whether their departments have done things.

**Q8 Chairman:** That is a very good answer, thank you for that. I just wonder if one of the problems is that it is not just politicians who do not take this subject seriously, it may be permanent secretaries. It is not nationally high profile politically, either with a big or small 'p'. I felt this when I read on page 19, paragraph 2.7: "22% of the contract managers surveyed considered that they did not have enough time to perform their contract management responsibilities well. . . ". I wonder whether these people are either not senior enough or have not been given enough time to do their job probably.

**Mr Smith:** It is a big issue. The first thing, which is perhaps peculiar to say, is where does contract management sit. When I came in 15 months ago, and I came in as Head of Profession for Procurement but also the PPM across Government, I asked some basic questions certainly with regard to the procurement profession: "How many do we have? What does it cover? How are we improving capability?" The answer to those first two questions was, "Actually we could not say how many we have or what it covers". We can now, by the way. That comes to the point I was going to make which is

contract management is a part of procurement. The emphasis in the past, and indeed in private industry, this is not peculiar to Government in my experience, is that procurement has historically been seen as letting a contract, let and forget, "We will let it, our problems are over". Contract management has not been seen as part of procurement.

**Q9 Chairman:** It should be let and managed is what you are saying.

**Mr Smith:** Absolutely. Of course, procurement is right from creating what the outcome is you want to deliver through the procurement to the completion of delivery, so it includes contract management. It was not explicitly a part of the procurement profession in Government, it is now an explicit part.

**Q10 Chairman:** We found that with PFI in the past, a weakness in management. One aspect of this is what happens if these people under-perform. What is rather worrying is we read in paragraph 2.19 at the top of page 23 that a third of contract managers are not routinely enforcing payment deductions when suppliers under-perform. Here you have got suppliers under-performing and a third of your managers not deducting. What is going on here? This would not happen in the private sector, would it?

**Mr Smith:** Oh yes, it would.

**Q11 Chairman:** It would, would it?

**Mr Smith:** Yes.

**Q12 Chairman:** Tell us.

**Mr Smith:** I agree with the vast majority of the findings and the recommendations, but I do think that in terms of the application of penalties there are obviously situations where we must apply penalties in contracts that have been written in if they are not being delivered. What this says is that 37% do not always apply penalties and I do not find that surprising. In fact, the application of routine penalties between a supplier and a customer is a sign of a poor relationship in my view. I do not often quote the NAO in terms of their reports but back in 2006 the NAO did a report into the MoD when it actually quoted as good practice, I think it was Toyota, the Queen Mary 2 procurement, I cannot remember, two customers who had not used contractual penalties. I have to say that is my experience. I have taken on in my business life massively onerous liquidated damages penalty clauses and I have had situations where they could have been used against me but because of the relationship I had with the customer and because we were focused on getting the right thing for the project it was not used. Having said that, of the eight contracts that are in this report that were looked at in detail, five of them have got service credit terms in there and all five have used those service credit terms. These were eight contracts picked at random out of the 123 that were reviewed. I do not find that peculiar. I do believe there will be instances in Government where there are obviously cases where they should have applied contractual penalty.

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14 January 2009 Mr Nigel Smith

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**Q13 Chairman:** That is your judgment, that is fine. I was warned that you might be giving an answer like that by the National Audit Office before we had this conversation. Perhaps I could ask Mr Burr or the Director to comment on this. You found that some people quite liked to be held to account.

**Mr Burr:** There clearly is a balance to be struck between showing you mean business and you are not going to be messed around on the one hand and maintaining a constructive relationship with the contractor on the other.

**Ms Brackwell:** From the survey of suppliers, the response we got was that 80% of them did feel that the incentives did encourage them to perform. Some of them commented that they felt it was a sign of a healthy, slightly combative relationship but albeit a positive one when deductions were applied.

**Q14 Chairman:** Does it worry you, Mr Smith, that we read in paragraph 2.26 that 41% of contract managers have not tested the value for money of new services purchased under a contract? Is that normal?

**Mr Smith:** I do not think that is normal, no. Testing value for money and benchmarking at certain points of the contract is an important requisite of large complex contracts. The issue is whether or not it is in the contracts in the first place and in many cases it is not in the contracts in the first place. A lot of guidance that we have recently put out, and will be putting out, will focus on making sure we build it into the contract where there is regular benchmarking, there are opportunities to test the contracts. In my experience, on the large contracts, many of which you have looked at as a Committee, whether they be FM contracts or the like, there are usually benchmarking opportunities. The large contracts like Aspire, things like that. There is some very good practice out there for benchmarking and testing value for money. I am not going to sit here and try and defend that percentage that is not looking to test value for money. The bit I am most concerned about is where there are changes because where there are changes in contract and they are not assessing value for money, that is the problem. Assessing value for money in a contract where there is no opportunity to make changes, the problem there was when the contract was let.

**Chairman:** That is a fair answer.

**Q15 Mr Bacon:** Mr Smith, I would like to ask first about the point in paragraph 2.5 about the number of contracts where there was no documented plan for managing the contract. It says there: "There was no documented plan for managing 28% of contracts". You mentioned earlier that the problems you face are not for the want of advice, in fact there is world leading advice, which is all very well but it does make you wonder whether to laugh or cry since with so much good advice around you would hope some more of it would have been taken up. Can I just clarify this point about having a documented plan for managing a contract. Is it included in this legendary advice that it should be considered pretty much standard, *a sine qua non*, where you have got

an important contract above a certain value that there should be a documented plan for managing the contract?

**Mr Smith:** It is in the advice, although I have to say I think the advice needs to be made sharper.

**Q16 Mr Bacon:** I can understand how in a small value contract you might not want to, but what I am really asking is, is it standard if you have got an important contract that there should be a documented plan for contract management?

**Mr Smith:** I believe it should be standard. Is it standard in the private sector, the answer is no. The private sector is probably better than the public sector, but the private sector sees contract management without any shadow of a doubt as one of its key areas of weakness. There is a very big report being done at the moment by the International Association for Contract and Commercial Management which looked at 10,000 private sector companies. I cannot tell you too much because it has not been published yet, but basically their conclusion will be that this is one of the big areas of process weakness in private industry. In my experience, if I ask myself the question did I always have a documented plan for my complex contracts in terms of contract management, probably not, I had parts of it. Should there be one? Yes, and we are going to make that absolutely specific in new guidance which builds on our joint guidance that came with this Report which will be out by April.

**Q17 Mr Bacon:** I hear what you say about the private sector, of course, but I am asking about the public sector. When you say the advice is not sharp enough, are you saying that it is just not clear enough in black and white, "This is one of the 16 things that you must do when you are letting a contract"?

**Mr Smith:** Yes, I think I am. I have got to say I think the advice is reasonably clear. We have picked this out as an issue in the Procurement Capability Reviews. We have also picked it out in the other reviews that we do in terms of assurance, particularly on the ICT category with major suppliers where we are looking at the Performance Improvement Plans of 15 major suppliers to Government which represents about 40% of total spend on ICT in Government. We are sharpening it up by those Performance Improvement Plans. The guidance needs to be improved, but basically we have got to make sure that people understand this should be done, it is about capability, getting the right people in place and right governance in place as well.

**Q18 Mr Bacon:** One of the things that has caused me to nearly despair, particularly in relation to the procurement of professional services, which is one of your categories, is there has been a profusion of advice for many, many years and yet what you talked about in terms of letting contracts being seen as the point at which you stop rather than the point at which you start, as it were, has been referred to so many times in the purchase of professional services, starting a bit earlier with the question of whether you

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need to go outside and selecting people who have got the right skills, making sure you procure properly, making sure you project manage properly, making sure you evaluate properly, that arc is all part of the contract management process properly understood.  
**Mr Smith:** It is.

**Q19 Mr Bacon:** And that has been said time and time and time again, including reports from the NAO as recently as 2006 and again in their report on purchasing professional services in 2001 and in the Cabinet Office study they did in 1994, which was led by your predecessor when he was at the Efficiency Unit in the Cabinet Office, and then I hear you say that you have got world leading advice. That was why I nearly laughed, because I think what is it about these very bright people running government departments, and we see them week in and week out, these permanent secretaries, that makes it so difficult for them to grasp the importance of doing what has been laid out clearly in report after report after report.

**Mr Smith:** The good news, I think—

**Mr Bacon:** I was not asking you about the good news, I was asking you what is it about these people.

**Mr Griffiths:** You would not be.

**Q20 Mr Bacon:** I will come on to the good news. I just want to know what is it that makes it so difficult for them to grasp the importance of doing it rather than seeing it as advice that is sensible and doing nothing.

**Mr Smith:** Contract management is difficult and it is the reason the private sector has such a problem with it. It is difficult to do. It requires a process, the right people and a different way of doing things. I cannot give you an answer to your question, to be frank, other than to say I do believe that permanent secretaries, my colleagues, round the table do understand this now. I think the Procurement Capability Reviews have been tremendously powerful in getting them to understand this. In the Report it talks about DWP and Leigh Lewis is an exemplar in this; he gets it. More and more permanent secretaries that I deal with get it.

**Q21 Mr Bacon:** I am pleased to hear that. To keep Mr Griffiths happy, can you now utter the sentence you were going to utter about the good news?

**Mr Smith:** The good news is that there are a great many examples of good practice in Government on major contracts. If you look at the eight contracts in the NAO Report, I was encouraged. There are some reds there and some amber/reds and if you go and have a look at our RAG status on the Procurement Capability Reviews, which is on our website, you will see a lot of reds and amber/reds. We did not pull our punches here at all. If you look at this, there are 88 indicators here and of those 88 we have got 51 of them that are green or green/amber. What does that mean? Green is absolutely best in class. Green/amber is very good process with one or two things to be done. To get 51 out of 88 on these indicators I think is good. The significance is if you look at the ones we are not doing well on, planning and governance,

which is what we were just talking about, and supplier relationship management, those two areas are the two most consistent areas that have come out of the PCRs which they have got Performance Improvement Plans on. I think you can take some comfort from the fact that, yes, there are going to be supplier cock-ups in the future, I am absolutely sure, but you can say the processes are getting much more consistent now and certainly it is on the top table.

**Q22 Mr Bacon:** A couple of questions. What about risk registers? It says in paragraph 2.21 that 30% of contracts dealing with personal or security information did not have a risk register. This Committee went to Heathrow Airport and met with Sir David Omand and HMRC in relation to risk management several years ago, about three years ago, because he, in addition to being security co-ordinator, had a risk management role. Who was his successor in that risk management role? Is it still somebody in the Cabinet Office, or is it you? Second, how can you have such a high percentage where the contracts are dealing with security information or personal information where there is not a risk register?

**Mr Smith:** To answer the first question, it is not me. I will get back to you on who it is,<sup>1</sup> I cannot tell you. On the second question, yes, that is worrying, but—

**Q23 Mr Bacon:** He was talking about risk registers as a thing you had to do in order to sign the Statement of Internal Control. In order to sign a Statement of Internal Control the permanent secretary had to have a risk register. This was kind of tattooed on your forehead when you became a permanent secretary.

**Mr Smith:** There are risk registers in every department, the issue is whether or not it has got all of the data security issues on the risk register is the point the Report is making. I believe that is an issue. There is a lot of work underway on that. It has got Gus O'Donnell's involvement and I have been involved with Gus. As recently as two months ago I invited the top 15 suppliers to Government in, these were the chairmen and chief executives, and said quite clearly to them that we had to improve the process we had on handling sensitive data. We have put a new model contract out that is mandatory. I know that is a word you like to hear, it is mandatory, and if it is not in the contract it is going to be put in the contract.

**Q24 Mr Bacon:** If you want to send us more of that answer in a note, that would be very helpful.<sup>2</sup>

**Mr Smith:** Will do.

**Q25 Mr Bacon:** In 2.15 it says that there was regular collection of performance information and discussion of performance with suppliers but that the exception was the Foreign and Commonwealth Office whose contract with Hogg Robinson Travel Group contains no performance metrics and there

<sup>1</sup> Ev 12

<sup>2</sup> Ev 12

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was, therefore, no formal way of measuring supplier performance. My question is, does it surprise you that the exception was the Foreign Office?

**Mr Smith:** If your question is, is the Foreign Office a good or a bad procuring organisation—

**Q26 Mr Bacon:** Does it surprise you that the exception is the Foreign Office? It does not surprise me at all, I am just wondering whether it surprises you.

**Mr Smith:** How I would answer that is if you would like to—

**Q27 Mr Bacon:** You answer “yes” or “no”.

**Mr Smith:** If you have a look at the Procurement Capability Review assessment of the Foreign Office, which is coming out in about six weeks’ time, I think, you can make your own assessment of my view of the Foreign Office general capability.

**Mr Bacon:** I shall look forward to that.

**Q28 Chairman:** We sometimes make this point to the Foreign Office and I think that is a fair question to ask. On this point of the risk register, why did the Driving Standards Agency not have a risk register when their contractor lost their disks? We see this in paragraph 2.23. There is an obvious risk there and no risk register.

**Mr Smith:** All I can say on individual instances is I do not have knowledge about every contract or every situation.

**Q29 Chairman:** No, of course you do not.

**Mr Smith:** Generally speaking, the issue of having the appropriate things on the risk register—you are not allowed everything—not that you have a register but you have a contingency plan and a mitigation plan which is there to mitigate those risks, that is an issue which has been identified and there is a lot of work underway. I think we will see some improvement.

**Q30 Chairman:** I think the Treasury want to comment.

**Ms Diggle:** Sir David Omand’s project finished, reached a conclusion and then was mainstreamed into guidance about what accounting officers should do, how SICs should be drawn up, how risk registers should be used all the time. It was deemed better that it should be mainstreamed as part of the general guidance. Whether it is being used is a different matter, of course, but that is what was done.

**Q31 Mr Bacon:** You are saying it is part of this world leading advice now?

**Ms Diggle:** Yes, it is.

**Q32 Mr Bacon:** What a relief!

**Ms Diggle:** It is mostly used, I see it used visibly a lot.

**Q33 Mr Griffiths:** I am very pleased to hear that Leigh Lewis gets it. Who does not?

**Mr Smith:** I think that is a very unfair question and I am certainly not going to come up with names. Generally speaking, I think the people I saw who did not get it when I came in 15 months ago are starting to get it.

**Q34 Mr Griffiths:** Who are you coaching then?

**Mr Smith:** The vast majority of my colleagues do get it and are involved personally in some aspect of procurement and generally the commercial environment in their departments.

**Q35 Mr Griffiths:** It must be a matter of serious public concern to know who is getting it and who is not getting it.

**Mr Smith:** It may or may not but I am not prepared to talk about individual names. What I would say is there are processes of improvement underway in every department.

**Q36 Mr Griffiths:** Well, you raised the individual name.

**Mr Smith:** I did because it is raised in the Report specifically about DWP. I was asked a question about permanent secretaries’ involvement so I mentioned Leigh Lewis, who is obviously heavily involved and is mentioned in the Report.

**Q37 Mr Griffiths:** Are the Foreign Office getting it?

**Mr Smith:** As I said before, you will see when we publish the PCRs on the Foreign Office that there are issues which are being addressed and it does have the involvement of the permanent secretary, yes.

**Q38 Mr Griffiths:** How important is it for contract managers to have a professional qualification?

**Mr Smith:** First of all, it is not unusual, in the private sector most contract managers do not have professional qualifications and that is the way it has been historically. I do not believe professional qualifications are actually the issue. Some of them do, some if they are in CIPS, but I would certainly not say that Chartered Institute of Purchasing and Supply—CIPs—is necessarily the appropriate qualification for contract managers. What is important is whether they get the right learning and development, the right training, the right community is established so they can learn from best practice. That is another part of the Report where OGC has got some recommendations that it is working on.

**Q39 Mr Griffiths:** If you can look at table 11, page 19, where more than 10% of contract managers have got experience of one year or less and are managing contracts with an annual expenditure of half a million pounds a year, how many of them will have no experience of managing such contracts?

**Mr Smith:** I have no way of telling. One of the issues that I mentioned right at the start when I talked about me as Head of Profession is contract managers are now part of procurement, we have mapped them into role profiles, we are identifying them as individuals so we can engage with them on learning and development, we can look at skills and

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experience. We have got a workforce planning plan, which I was only discussing with my permanent secretary colleagues this morning which they have signed off, which talks about talent management, career development, succession planning, learning and development and also rewards, which is also important, to get a rewards strategy which supports it. No, I cannot tell you how many are under a year.

**Q40 Mr Griffiths:** Could somebody be appointed within Whitehall as a contract manager tomorrow without contract management experience?

**Mr Smith:** Yes, they could.

**Q41 Mr Griffiths:** What is the worst scenario then?

**Mr Smith:** The worst scenario is if that person gets appointed to a really sensitive contract.

**Q42 Mr Griffiths:** Where would they have come from?

**Mr Smith:** There is a whole range of people, for example, in the wider commercial area, they could have finance experience, they could come from procurement policy, a whole range of areas.

**Q43 Mr Griffiths:** Is there anyone from when you were wearing your private sector hat that you would be concerned about that was coming from a background from the ones you have mentioned and listed?

**Mr Smith:** Did I have examples in my private sector background?

**Q44 Mr Griffiths:** You have told us various credible backgrounds that people might have. Are there any with backgrounds that you would have found in the private sector not to be so credible that need to be addressed?

**Mr Smith:** I am sure there are people managing contracts in the public service who do not have the right experience or background.

**Q45 Mr Griffiths:** That was not my question.

**Mr Smith:** I am missing the point.

**Q46 Mr Griffiths:** My question was really focusing on people who are made contract managers tomorrow. Are there any people who do not have that range of background? I am thinking rather than the Classics, for instance.

**Mr Smith:** I see what you mean. I would find it very surprising if we had too many Classics scholars as contract managers.

**Q47 Mr Griffiths:** Would one not be too many?

**Mr Smith:** One would probably be too many, although I have many colleagues who are Classics scholars.

**Q48 Mr Griffiths:** There is nothing wrong with that and that is why we are focusing in 2.10 on having a professional qualification or experience.

**Mr Smith:** This chart, which shows that over 40% have got ten years-plus experience, is not typical of the private sector. Ten years-plus experience at over

40% is an incredible statistic, I have got to say, it is very high. The issue is does ten years in a job give you ten years' experience, if I can put it that way. That is why we have got to get in with these people, understand their skills and capability and work with them to improve on it.

**Q49 Mr Griffiths:** How important do you think it is that existing contract managers undertake some sort of current training?

**Mr Smith:** Absolutely vital. There is a lot of training that goes on. I know PFI is a matter for the Committee on a regular basis, but within PFI—

**Q50 Mr Griffiths:** If it is absolutely vital why have 60% of organisations surveyed not provided any structured training programme? That does not seem absolutely vital to me.

**Mr Smith:** I agree. That is why that is a principal recommendation in this Report for OGC and OGC is extremely active on this at the moment. I keep coming back to it, but the first thing you have to do is identify who these people are. You have to have them as part of the community and then you have got to provide the right training. OGC will not itself do the training. What OGC will do is get the right structured training using best practice and, in fact, we have a pilot with DCSF and are using the Lloyds TSB best practice that is quoted in here.

**Q51 Mr Griffiths:** That is reassuring but it is of concern if you do not know who they are. Is that not a quick thing to find out?

**Mr Smith:** That is what we now know because we have redefined procurement to include contract management.

**Q52 Mr Griffiths:** What is your target date for having that 100% contract management training, that vital training?

**Mr Smith:** I cannot commit to a date at the moment because I want to make sure anything I commit to I can deliver. The training will be delivered by the departments, not by OGC. The issue is identifying who these people are and agreeing, as we have done this morning, what are the career development plans, what are the skills required and what is the continuous professional development. In this plan agreed this morning, and it was not because I was coming to the Committee I hasten to add, we have agreed 50 hours of professional development which is a requirement for people in the procurement profession; an explicit statement they must have this. It is our job to make sure that there is the appropriate learning and development available and we are working with the National School of Government, with CIPs, with a whole range of outside private bodies, and also using the Lloyds TSB example which is quoted in the Report.

**Q53 Mr Griffiths:** How important is it below board level that organisations have an individual with overall responsibility for contract management across the organisations? This is 2.4.

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**Mr Smith:** I am absolutely clear, you must have clear governance for contract management. The Report says that there should be one person in the department in charge of contract management, I do not fully agree with that.

**Q54 Mr Griffiths:** I thought you had signed off this Report.

**Mr Smith:** I have. I have signed off the Report but I sign off the Report for factual accuracy, I do not sign off the Report to say I agree with everything that is in there because I cannot change it. This is not a big thing because I think the general thrust of what the NAO Report says is right. A single point within a department for contract management policy, practice and capability I absolutely agree with. A single point for contract management for all of the different contracts going up to the same point I do not necessarily agree with because it is not necessarily aligned to the organisational structure of the business. The thing it must have is clear governance and that we agree on absolutely.

**Q55 Mr Davidson:** I wonder if I could start from the point of view that there is always a balance in the relationship between the public sector and its supplier which is akin to that, in a sense, of the predator and its prey and quite clearly in some ways the relationship is a zero-sum, that the predator if they get more out of the system and deliver less are better off and the public sector is worse off. Can I just clarify in these circumstances whether or not in paragraph 2.6 the equivalent of 2% of annual contract expenditure being spent on managing the contracts is generally considered to be sufficient given the risks involved? Is there a target figure? Is there a number of criteria that take into account the complexity of the contract and so on and so forth? Give us a benchmark about what it is reasonable to spend managing a contract.

**Mr Smith:** I do not think I can answer the question, not because I do not want to but I do not think I have enough information. Certainly I would agree with you that the amount of resource you put on to it is entirely associated with the level of risk and the importance of that contract to your organisation. CIPS, certainly in one report I do remember in a very high risk important contract there is a suggestion that you should spend between 10% and 15% of the contract value on contract management in the first three years. That is one I can specifically remember which then basically says you are spending about 5% a year. I do not think that is a magic number. The issue is whether or not we are spending the right amount of money on the right people and we need to have a look at that department by department.

**Q56 Mr Davidson:** Over the years when we have been looking at, say, defence contracts for example, I think we have accepted spending is of a higher percentage front-end, as it were, before steel gets cut and things like that on the basis it avoids reworks. That sort of 15% figure has become a reasonable norm. Are you saying there is nothing like that in any of this? When I look at paragraph 2.8 where it is

talking about the contract manager for the Ministry of Justice managing this contract and two others and so on, I wonder whether or not the supervision of that contract is not under-financed. I wonder on what basis somebody arrived at the assumption that was the right mechanism to have and the right cost to lay out. As you have indicated, surely people in departments who do not get it, as you have put it, ought to have some sort of guidance about what an appropriate level of spend in managing a contract ought to be.

**Mr Smith:** I think we should certainly give guidance which says that there should be an appropriate level. It would be extremely difficult trying to come up with the percentage contract by contract.

**Q57 Mr Griffiths:** Yes, but you did say it ought to be at an appropriate level and nobody is going to say, "We advise you to have this at an inappropriate level".

**Mr Smith:** That is a statement of the obvious.

**Q58 Mr Griffiths:** What is an "appropriate" level? If you are not giving them any guidance then, frankly, that is useless advice.

**Mr Smith:** The existing advice, which is our joint advice, is basically we have the right people with the right resource, which is an obvious statement I suppose, but based on risk and value for money and importance to the department. We are looking to develop that in our guidance coming out in April. I will take a look at that issue in our guidance. I have not got an answer on that.

**Q59 Mr Griffiths:** Looking at 2.8, does it seem to you that enough money is being spent at the Ministry of Justice on that contract on courts security and the two other contracts? Reading this as it is written, it seems to me that person supervising those contracts is overloaded and insufficient money is spent on that. I wonder whether or not that leads us on to assume that the Ministry of Justice is one of those that does not get it.

**Mr Smith:** You are going to lead me into saying which ones get it and which ones do not.

**Q60 Mr Griffiths:** Yes, exactly.

**Mr Smith:** The Ministry of Justice is going through a fundamental restructuring of its commercial activities, which I absolutely support.

**Q61 Mr Griffiths:** So that is a "yes" then. Given what we have got there, am I right in thinking the Ministry of Justice in that contract is not providing adequate funding for that supervision and clearly they have been either badly advised or have advised themselves badly? It is question of how they got into that position and this comes back to the question about guidelines about what is reasonable in what circumstance.

**Mr Smith:** I think you have got to look at every individual circumstance. As far as the Ministry of Justice is concerned, I believe that has been published or is about to be published on PCRs. Contract management and supplier relationship

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management are two absolutely key recommendations which are part of the action plan. If you do have a look at the review which the NAO did of this particular contract, I would have to say to you on things like contract development they actually came out of it quite well, and managing performance, managing relationships, they were amber/green. The issue is whether they have got enough and I would have to say it probably seems to me they do not have enough people on it.

**Q62 Mr Davidson:** Which leads me back to the point I was making earlier. Can I move on to the question of relationships. I am struck by this first point in paragraph 2.12: “contract managers and suppliers surveyed were positive about their working relationships”. I can remember in local government a while ago there were lots of people who were very positive about their working relationships and in some cases ended up going to jail because while they were positive about their relationships they were corrupt. Being positive is not enough, in a sense. Nowhere in the list of strengths, as it were, how it is measured, does it place sufficient emphasis on the question which is down in one heading as continuous improvement and challenging behaviour, as it were.

**Mr Smith:** Yes.

**Q63 Mr Griffiths:** To some extent this relates to the question of lack of penalties. It is very easy to have a relationship that is comfortable with a supplier if you are just sitting on your behind, and it is very easy to have a comfortable relationship with your client if he never asks you any questions and you take them regularly for golf. How exactly do you make sure that there is a creative tension managed between supplier and supplied, between predator and victim, that ends up with the best deal for the public purse?

**Mr Smith:** You do it through a whole range of mechanisms, if I can just quote a couple. In ICT, which represents out of this Report around about a third of the 12 billion, and by the way service contracts are not 12 billion in Government, in these categories the total is around 23 billion, 12 billion is purely the sample which is in this Report, if you have a look at what we are doing in terms of the ICT category, which is the biggest category, we have what is called the CAF process for the top 15 suppliers which represents about 45% of the total spend in this category in Government. We have a CAF process which is very mature now, it is done every six months. It is a very detailed assessment against 12 indicators which includes performance, value for money, relationship. It is overviewed by the CIO Council and also by OGC, so it is not done in a cosy relationship between the Department and the supplier, and there are Performance Improvement Plans and at some future point I would love to show you what those include. This is a pretty rigorous assessment.

**Q64 Mr Davidson:** If we look at paragraph 2.13, right down the bottom, it says an example of good practice is the Land Registry and Hewlett Packard,

genuine trust and respect on both sides and a ‘no blame’ culture. We then turn to paragraph 2.20 at the top of the second column and they had half a day’s downtime when the computer system was unavailable and they got a payment deduction of £440 which does not seem very much to me. ‘No blame’ is quite good if you are the one who is getting blamed. If I have ever done anything wrong I am very keen on a ‘no blame’ culture, but I am not quite as keen on it the other way round. This surely can just lapse into cosiness. If we look at 2.19 where there is mention of a substantial number, almost 40%, not invoking deductions it seems to me these relationships can become too cosy by half and the public sector is being ripped off by sharks.

**Mr Smith:** I am certainly not suggesting that we should not have hard-edged incentives, penalties in contracts, I absolutely agree that we should. The issue that I was trying to make right at the start is that I did not find it surprising that 38% of the commercial directors and heads of procurement said they did not always invoke penalty clauses. I do not find that surprising. Not always, it suggests they do some of the time. The issue for me is what is their overall value for money for a particular contract. I agree with you, it should not be a cosy relationship, it should be a challenging relationship.

**Q65 Mr Davidson:** The final point in the second sentence of that section there that concerns the invoking of service credits would damage the organisation’s relationship with the supplier seems to me to be a recipe for soft-peddling. If we had down there that concerns that arresting people would damage the police’s relationship with criminals, you would not accept that for a moment, would you?

**Mr Smith:** Absolutely. In that circumstance I am not going to try and defend that. Quite obviously if the only reason people are doing it is not to upset the supplier, that is bloody stupid, but I do not honestly believe that is generally speaking the case. In my view there are many reasons why you would not invoke a penalty if you were working in a principle of continuous improvement with a supplier with a good relationship. I can give you many, many examples both within the guidance that we have but also in practice on the assurance that I get involved with where we are looking at incentivisation, a balance between incentivisation and penalties. That is particularly important when you are looking at long-term contracts.

**Q66 Mr Davidson:** In the same way that deductions are not always made, can I just be clear whether or not incentives are always made? Are there a whole number of circumstances where incentives that could have been applied are not taken by the service provider, or is this in some way a one-way street?

**Mr Smith:** I do not think I can answer that generally, I would have to look at particular contracts. I can only give you a view. I am sure that we have not got the balance right between incentives and penalties and active management, I am absolutely sure of that. What I am trying to say is that we have got a lot

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going on in the work we are doing on capability, the work we are doing on guidance, and we do have some excellent examples in Government. This is not a complete basket case, but there are some basket cases I have seen even over the last few months, and I get involved.

**Q67 Mr Davidson:** It would be helpful if we had a list.<sup>3</sup>

**Mr Smith:** Absolutely.

**Q68 Chairman:** Would it be a fair comment to say, Mr Smith, that your Department has not monitored major suppliers much beyond the IT sector?

**Mr Smith:** I think that is a reasonable comment with the exception of consultancy where we do have some monitoring.

**Q69 Chairman:** Does that worry you?

**Mr Smith:** It does, and that is why we have a comprehensive programme underway. We are expanding our CAF assessment into software, so not just into hardware and services but also into software, into the full gamut of professional services. We have set up six other categories for collaborative procurement where we are going to do supplier assessment on our major suppliers to Government. Those are things like office solutions, energy, food, construction and a number of others. Yes, we have got a very comprehensive programme underway.

**Q70 Mr Mitchell:** I think this business of contracting out government services has been a fashion for something over three decades now and the argument has always been that we save money. At the end of the day can we quantify the savings, say how much each department that has gone in for these kinds of contracts has saved over a period?

**Mr Smith:** No, I cannot, I do not have those statistics. I can make an observation. I do believe that when we are looking to outsource services we should understand why we are doing it and we should benchmark the value we get from it.

**Q71 Mr Mitchell:** But we are doing it to save money basically.

**Mr Smith:** To save money and also to improve service in a lot of the cases is the original objective.

**Q72 Mr Mitchell:** Yes, but it is also not to employ people as civil servants, is it not, on civil service pensions?

**Mr Smith:** That may be the case, I would not want to comment on that. Certainly as far as insourced and outsourced, I do believe, and I have got discussions underway with the CIO Council, we should have a more structured approach very often to have a look at why we are doing things.

**Q73 Mr Mitchell:** Yes, but at the end of the day we cannot quantify how much has been saved by this massive transfer of services and functions to the private sector from the public sector.

**Mr Smith:** I cannot aggregate it across government, no. I do know many of these contracts have been looked at by the NAO. In preparation for this Committee meeting I looked at rather a large number of them, and in many of those cases they do establish that there has been significant value for money savings. The idea that outsourcing is good and insourcing is bad is not a particular philosophy that I buy into. Indeed, I think that you should strategically decide what you wish to insource and what you wish to outsource.

**Q74 Mr Mitchell:** Outsourcing must be assumed to be inherently cheaper. Do you impose pay and conditions in contracts?

**Mr Smith:** I have to say in the contracts that I have seen I am not aware of any such imposition. Basically, by its nature what you are doing is contracting for an outcome, so you are not contracting for the cost elements of that outcome, you are contracting for an outcome. I am sure there are many cases where there are significant value for money gains to the public purse by outsourcing.

**Q75 Mr Mitchell:** But also cutting costs by employing cheap labour.

**Mr Smith:** I have to say I am getting into non-quantifiable statements here. I do not think that is necessarily the case, I have to say. In my private sector experience outsourcing is absolutely not about cutting the wages of the people. In my experience, successful outsourcing is about using those people much more efficiently with better business processes and support.

**Q76 Mr Mitchell:** Although it does have the effect of cutting wages for people delivering services.

**Mr Smith:** Not always.

**Q77 Mr Mitchell:** Let us move on. Is it your impression that departments vary in attitude, some are enthusiastic about this outsourcing and some have to have it pushed on to them?

**Mr Smith:** There are certainly some departments that have embraced it in a much greater way. I just leave it at that. If you look at some of the best practice people as well DWP is an example.

**Q78 Mr Mitchell:** There must be some who are reluctant to embrace it, must there not? The fact that they have not consistently been concerned at delivering value for money must indicate a certain amount of lackadaisical implementation.

**Mr Smith:** Actually it is the subject of part of the Operational Efficiency Programme which is due to report in the Budget in March being led by Martin Read. This is one of the particular strands which is looking at the effectiveness of back office support sharing. It is not specifically about outsourcing but obviously has a big implication for outsourcing. It is about shared back office support finance procurement, *et cetera*. It is a matter of some debate.

<sup>3</sup> Ev 13

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**Q79 Mr Mitchell:** At 3.10 the Report says that there is inadequate collaboration and sharing of information on suppliers between departments and you said you are trying to secure more effective collaboration and sharing of information. In the light of that, can you tell us whose fault was it that the SATs testing was so disastrous? Here was a firm which proved not up to the job. Who employed them? Who vetted them? Why were they used?

**Mr Smith:** I know something of SATs obviously because of the Sutherland Inquiry. I do not know all of the detail. The Sutherland Inquiry stated quite clearly that the procurement process was sound.

**Q80 Mr Mitchell:** Was your Department consulted?

**Mr Smith:** Not as far as I was aware. It may have been consulted for information. Certainly OGC is referenced in the document. It talks about OGC's involvement through the Gateway process. If we had more time I would love to discuss that because the OGC involvement was at one stage and it did actually say that the procurement strategy was sound and, indeed, I have looked again and it was.

**Q81 Mr Mitchell:** Its results were disastrous.

**Mr Smith:** No, sorry, the procurement strategy. The issue was the supplier that was selected failed to perform.

**Q82 Mr Mitchell:** Yes.

**Mr Smith:** That is not about the procurement strategy. That is about the selection of a particular supplier.

**Q83 Mr Mitchell:** That you are saying was the responsibility of the department.

**Mr Smith:** Absolutely right and I am actually conducting a lessons learnt for David Bell at the moment, looking at the process assurance parts of government. There are some tweaks we can make to process.

**Q84 Mr Mitchell:** Will that supplier be used again, having made such a cock-up in that area?

**Mr Smith:** It is not for me to make that judgment.

**Q85 Mr Mitchell:** It is, surely, if you are going to co-operate and share information.

**Mr Smith:** Yes.

**Q86 Mr Mitchell:** And you are overseeing the whole business.

**Mr Smith:** Yes, and in terms of the major collaborative categories we will assess suppliers but it is actually a departmental decision to employ a particular supplier—my responsibility is to make sure the right processes assurance and information are there on cross-governmental issues; it is for the department to make those judgments. Having said that, if I saw a department employing a supplier which I had serious concerns over, obviously I would go and speak to them, but it is the department's responsibility.

**Q87 Mr Mitchell:** I was just wondering how information is circulated that this is a bum supplier.

**Mr Smith:** Of course, on this particular issue there was not a mechanism for this supplier to be shown up because the only collaborative category where we do systematic supplier assessment is in the ICT. As I have explained, we are expanding that significantly.

**Q88 Mr Mitchell:** Okay. Let us move on to the Educational Maintenance Allowances cock-up; who was responsible for that?

**Mr Smith:** I do not want to sound defensive here but I think you are asking me the question was OGC involved. I know something of the Educational Maintenance Allowance—

**Q89 Mr Mitchell:** Who awarded the contract?

**Mr Smith:** We were not actually involved in terms of either the Gateway process or specifically but I can tell you that I have looked at it and we have offered—and the offer has been taken up—to do a lessons learnt. So my department and I are actually going to look at this from a historical perspective to see what lessons can be learnt, but this was a procurement which was conducted by a department. There was a value-for-money case made at the time that this was let to Liberata. That value-for-money case was quite clear against the incumbent supplier; we have now gone back to the incumbent supplier. The issue that I am sure will come out of lessons learnt is actually how we managed that supplier during the contract, ie did we find out the problem early enough and did we do something about it. That is my gut view; we will find out.

**Q90 Mr Mitchell:** Mr Davidson took up the issue of cosy relationships developing and I see from 2.19 that 38% of contract managers whose contract allowed for service credit deductions did not use them. They were keen to give money for incentive payments, they were not keen to deduct for failures. That means, surely, something of a cosy relationship has developed.

**Mr Smith:** As I said before I do not find that surprising. It does say 38% did not always impose those service credits—not always—and I do not find that surprising for the reasons I gave before. There will be instances where we have not applied penalties where we should have applied penalties; I am absolutely certain of that.

**Q91 Mr Mitchell:** My final question. We had a phone call from a member of the public who said that the OGC had decided in 2005 that there should be only one construction contractor, limiting Whitehall construction contracts to one supplier. Under pressure the caller told us you had commissioned a review by Arup and this had, he said, recommended that there be three construction contractors and not just one, but the OGC are still sitting on the report and apparently want to stick to the one contractor, which again would be a cosy relationship. Is this correct?

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**Mr Smith:** I have no knowledge of it and it sounds absolutely amazing to me, how it has been described. I am sure that there is something in this which is perhaps slightly different.

**Q92 Mr Mitchell:** Can you check that?

**Mr Smith:** I will certainly check and I will come back to the Committee.<sup>4</sup>

**Q93 Chairman:** My colleague Austin Mitchell referred to a number of cock-ups by bum suppliers, as he put it so elegantly. My last question to you is do you have enough clout in Whitehall? Are you the gracious part of the constitution a bit like the Queen, you can advise, as opposed to the effective part, the Treasury, can order?

**Mr Smith:** If we are looking at individual contracts, can I pick up the phone and get the permanent secretary or whoever's attention I want to on a contract, yes.

**Q94 Chairman:** You can get their attention, they will answer your phone call, fair enough, whereas they may not answer Mr Mitchell's or my phone calls, but what happens after you have had the conversation?

**Mr Smith:** I have got to say I do not have one instance where I have recommended that something should be done when it was not done. I do believe I have clout; the issue for me is not whether I personally have clout because, with the best will in the world, I am going to get involved in only a small number of maybe highly sensitive contracts; the issue is whether or not we institutionalise the process whereby there is clout in the process so that when I disappear at the end of my term the clout does not disappear with me as an individual.

**Chairman:** Mr Davidson has one last question.

**Q95 Mr Davidson:** You mentioned a couple of times in responses to Mr Mitchell about producing reports on lessons learnt; it would be helpful if you could maybe give us a note indicating how many of these sorts of reports have been produced and rather than asking for them all ourselves it would be helpful if we could maybe have a summary of the general points that have been identified so that we can be clear in our own minds as to whether or not there is a series of different reasons why things have gone wrong or whether or not there are several consistent themes coming forward.

**Mr Smith:** There are two issues.

**Q96 Chairman:** He asked you for a note by the way.

**Mr Smith:** I know it was a note but before I let that pass by the thing I was talking about as to lessons learnt was where, basically, I have looked at something, it has been in the public domain, it has been a highly critical problem to government and I have offered support, particularly on the EMA situation, of OGC to do a lessons learnt exercise. It is not a systematic issue. What we do is have a look at lessons learnt which we build into policy, which we have done—that is where the *Main Causes of Project*

*Failure* document came from—and we also look at lessons learnt and common issues in the gateway process and also on our major projects programme. I am quite happy to give you an idea of where we pick out the strands of problems and how we disseminate it.<sup>5</sup>

**Mr Bacon:** I was going to ask one quick question to you and one to the NAO but I will ask you two now, one about Gateway, because in the Rural Payments Agency there was a whole series of internal reviews that hit red traffic lights as well as the ones done externally by the OGC when there was, as you know, a succession of red traffic lights. The answer one always gets is you have to understand the red traffic light does not mean you should stop—which I must say according to the Highway Code I always understood that it did, but that aside—it just means that you know you have got a problem and you must address it, and then of course a few months later you get another red traffic light and another one, and then finally you see this slow motion crash.

**Chairman:** It means drive faster.

**Q97 Mr Bacon:** It means drive faster, yes, which is exactly what happened in the case of the Rural Payments Agency. There has been a lot of discussion about whether Gateway reviews should be published and the answer always is the same—in fact I have had the same answer verbatim from different ministers, which shows at least they know how to copy and paste—as to why Gateway reviews should not be published. It seems to me that the burden is on Government to make a case for why they should not be anything other than public because the lessons are not being learnt, they are not being disseminated, they are not being spread and if they were much more public then far more people from informed journalists to parliamentarians to the public would be able to see what was going on and perhaps some of these slow motion crashes might have been avoided. When are you going to start publishing Gateway reviews? That is question one.

**Mr Smith:** Question one; there is a further one.

**Q98 Mr Bacon:** The second one is John Oughton, your predecessor, used to report to the Prime Minister on what he called 91 mission critical projects where he had quarterly to report to the Prime Minister on what was going on with them. I am just wondering is that still going on with you—it might not be 91 any more but is that process still taking place?

**Mr Smith:** Publishing Gateway reviews: can I just say that Gateway now is very different to Gateway then. I am glad you asked me about the Rural Payments Agency because I thought you might so I did my homework. There were four reviews by OGC, three of them were red, and some of the recommendations made by OGC were not adopted. At that time, if you look at the escalation, what happened was the double reds—

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<sup>4</sup> Ev 13

<sup>5</sup> Ev 14

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**Q99 Mr Bacon:** When you say the escalation you mean the driving faster.

**Mr Smith:** No, I am talking about escalation in actually making it public. The process was that if there were two consecutive reds and this was for a particular project, then we notified the NAO and the NAO in turn notified PAC. I have changed that process because those reds were actually about the urgency of recommendations, so you could have a situation where there was actually an absolutely critical recommendation, do it now, on a project, but actually the delivery confidence of that project was very good. It was not telling you, therefore, what are the projects about to be a train crash. What you want to know is, is this project in grave danger of not delivering to time, cost or outcome so we have changed the Gateway process—that is precisely what it has done. We have done a second thing, and this was done jointly with the NAO, and that is we have taken it down to a single red so now there is no place to hide. Previously to get two reds the average time was 18 months; there is an awful lot of problems can happen with a project in 18 months time. Now a single red gets escalated. I write a letter to the permanent secretary, it is disseminated to the centre of excellence on PPM, it is disseminated right across the department, it goes to the NAO, the NAO notify you, the PAC. I think that is one of the biggest changes of assurance to meet the point you are making. The issue of course it does not answer is why are you not publishing. I have to say as a citizen publishing things and public accountability seems a pretty good way of doing things, but I am not going to—

**Chairman:** You need not say any more.

**Q100 Mr Bacon:** We have got the quote.

**Mr Smith:** You have got the quote, thanks very much. There was another part of the sentence, if I could just make it known, purely to say that I do

think in commercial arrangements it often can be a defence to hide behind commercial sensitivities, but I do believe that in many cases they are real. I am not going to try and set government policy on publishing or not publishing; my role is to make sure that things are known within government, at the highest possible level, and you are asking me the question really do we stop. Can I say stop? I can say to the permanent secretary “This is not going to deliver, you have got to go right back to square one” and then I will have a conversation with him, when he has had a look at it. We are actually getting to the stage now where we are as close to getting to stop as we can. As far as 91 mission critical projects are concerned, no, we do not do 91 any more, we do 42. Those 42 are done in a very comprehensive way, they are done involving everybody with knowledge of the projects and they are done on a quarterly basis. So against a whole set of measures we are reviewing the top 42. I discuss those with permanent secretaries on a regular basis, I send those to the appropriate secretary of state, I send them to the Prime Minister and I circulate them within the departments. There is absolute visibility now, therefore, and more and more engagement with both ministers and permanent secretaries to use the information.

**Q101 Chairman:** That is a very important and very full answer and that concludes our hearing on a very good note, so we are very grateful Mr Smith. I will say that my clerk has informed me that in Turin red traffic lights are instructions, in Rome they are guidance and in Naples they are Christmas decorations. We do not want them to be Christmas decorations in Whitehall from now on.

**Mr Smith:** Indeed. Thank you.

**Chairman:** Thank you very much.

## 1. Supplementary memorandum from the Office of Government Commerce

*Question 22 (Mr Bacon): Successor to Sir David Omand, former Security Intelligence Coordinator*

In July 2007 changes were announced to the organisation of the Security and Intelligence function in the Cabinet Office. Robert Hannigan, formerly Director General (Political) at the Northern Ireland Office, took up the post of Head of Security, Intelligence and Resilience and acts as Security Adviser to the Prime Minister in the Cabinet Office. For further details of these changes please see: <http://www.cabinetoffice.gov.uk/newsroom/news—releases/2007/070725—security.aspx>

*Question 24 (Mr Bacon): Data Security Issues on Departmental Risk Registers*

Over the past year the Cabinet Secretary, Sir Gus O’Donnell, has personally taken forward a number of pieces of work across Government on data security issues.

The Prime Minister commissioned a review of government department’s data handling procedures led by the Cabinet Secretary, which was published on 25 June 2008 and can be read on the Cabinet Office website: [www.cabinetoffice.gov.uk/reports/data—handling.aspx](http://www.cabinetoffice.gov.uk/reports/data—handling.aspx). The review states that all government departments will ensure that new contracts with suppliers will include security clauses reflecting the measures outlined in the report. For example, staff should be trained in basic data security best practice, the secure transfer of data, the encryption of data held on mobile devices and the secure disposal of data.

On 17 November 2008 the Cabinet Secretary Sir Gus O'Donnell chaired a meeting with the largest suppliers to government on data security alongside Nigel Smith, OGC's Chief Executive, Iain Lobban, Director of GCHQ, and John Suffolk, the Government CIO. The aim of the meeting was to ensure that all the key government suppliers handle personal and sensitive data on behalf of government and are aware of their current obligations in respect of the new data security measures. On contractual matters Nigel Smith outlined the new security clauses, applicable to all contracts involving significant personal data, including for subcontractors. Accountability for ensuring information assurance lies with contracting departments and suppliers. Departments and suppliers are also responsible for auditing their processes and people to ensure that these requirements are actively met.

There is a mandatory Privacy Impact Assessment for all contracts involving personal information and an Annual Statement of Internal Controls will include the assurance processes for the management of information assurance related risks.

*Question 67 (Mr Davidson): Examples of where incentives have not been taken up by the service provider*

OGC requested details from Departments on the use of financial incentives in contracts. Responses highlighted that there are many cases where payment is linked to achievement of Key Performance Indicators, and fewer but still a good number of examples where Gainshare arrangements are used (where suppliers are encouraged to propose improvements and any savings are shared between supplier and customer). Risk/Reward approaches are also used (typically where a base cost is agreed, but the supplier's profit is linked to the extent to which they exceed agreed targets, service levels or performance indicators).

Where Gainshare or Risk/Reward approaches are employed, there does appear to be more likelihood of the service provider taking up the incentives; however, this is based on a small sample so cannot be taken to be representative. It may also be a reflection of the maturity of the approach to contracting or contract management in that organisation, the nature of the service being provided, or the degree of flexibility included within the contract for the provider to make changes.

No examples were put forward of cases where service providers have been entitled to payment for achievement of performance levels but have not taken up those payments. There were a number of examples of cases where there was the potential to obtain additional payment through 'over-achievement' but where service providers had not reached those standards. In some cases this was due to the contract and service provision taking time to reach a mature status, with the department anticipating the service provider becoming eligible for payment in the near future (eg HMT—Facilities Management contract, DWP—printing and stationery supply contract).

In other cases, in spite of the inclusion of incentives within the contract, the current levels of performance did not indicate that the service provider would be likely to reach the required standard to become eligible in the near future (Home Office—IT contract, DVLA—license/ product sales through Post Office). This raises the question of the effectiveness of the incentivisation approaches employed—it is possible that the return available to the service provider would not be sufficient to justify the effort required to make changes or improvements to performance.

*Questions 91–92 (Mr Mitchell): Update on Arup review*

Until relatively recent times government has owned and managed its own suite of forms of construction contract known as GC/Works. Early in the present decade it became increasingly apparent that those forms would need to be substantially rewritten to bring them up-to-date with more modern methods of procurement. Rather than simply commissioning a new edition of the forms, OGC was conscious of the fact that reports on the construction industry [such as Latham/Egan] had highlighted the proliferation of standard forms and the problems associated with them and so OGC examined whether an existing form would better suit the purpose of helping government take forward its improvement agenda. The NEC3 suite of forms was seen as the most compliant with OGC's Achieving Excellence in Construction (AEC) initiative and, subsequently, OGC supported government clients' transition to the use of those forms.

Over the last two years the authoring bodies of some alternative forms of contract have lobbied OGC to relook at their products as they asserted that recent revisions had made them compliant with the principles of AEC. This led to the appointment of Arup to carry out an independent study on behalf of OGC. The Arup report has concluded that that the two other forms of contract had also become compliant with the AEC principles.

On 11 December 2008 the Public Sector Construction Clients' Forum (PSCCF)—which includes the key government clients in Central Government and Local Government, as well as supplier representation—discussed the conclusion reached by Arup and was pleased to note the progress made by the other forms. However, PSCCF members strongly voiced their support for the continued standardisation on one suite of forms of contract and that this should be NEC3.

The notes of PSCCF's quarterly meetings are published as a matter of course on OGC's website ([www.ogc.gov.uk](http://www.ogc.gov.uk)). The report from Arup is also available there alongside the note of the PSCCF meeting held on 11 December 2008. The report had previously been shared with all the stakeholders involved in the study, including the Joint Contracts Tribunal (JCT).

The JCT, who own an alternative form of contract considered by the Arup study, is presently actively publicising the conclusion made by Arup. It was JCT's agent, Chelgate PR, that phoned the Public Accounts Committee immediately prior to Nigel Smith's appearance on 14 January 2009.

*Questions 95–96 (Mr Davidson): Themes arising from OGC's assurance processes*

#### PROCUREMENT CAPABILITY REVIEWS

Focusing on where a department's money is spent and how it achieves value from that spend, Procurement Capability Reviews (PCRs) are intensive independent reviews of commercial capability in the bigger spending government departments. At a strategic level, they assess procurement capability in departments against a framework of standards set out in the PCR model.

From the ten PCRs published so far a number of emerging themes have been identified both in areas for action and examples of good practice. Each department has agreed an appropriate improvement plans to address those areas that require action. A further six reports and improvement plans will be published by April 2009.

The emerging cross Government themes from the first wave of Procurement Capability Reviews (PCRs) are set out below:

<i>Key Themes (Improvement Areas)</i>	<i>Other Themes (Mixed Picture)</i>	<i>Key Themes (Positive Themes)</i>
Shortfall in highly capable commercial people	Commercial Strategy & business alignment needs to be developed	Good people in procurement, more professionalism
Shortfall in contract management skills and resources	Supplier Relationship Management is inconsistent	Strong Leadership, from Heads of Procurement
Lack of management Information	Need for greater knowledge management & sharing	Increasing commercial focus & experience at Board level
Performance not measured consistently	Category management could be developed further	Good processes and procedures, collaboration well understood
Difficulty influencing spend outside the core department		Departments are making impressive savings through procurement

OGC has put in place a number of initiatives to address the areas highlighted for improvement, for example:

- **Paucity of Management Information:** OGC runs the Public Sector Procurement Expenditure Survey (PSPES) that seeks to establish common definitions and record public expenditure of third parties particularly with regard to Government's collaborative procurement categories. This initiative encourages departments to collect and measure their spend data in order to control third party spend more effectively. It is also used as a basis for developing "Spend Data Improvement Plans". OGC through OGCBuying.solutions has also established a framework contract for the provision of external support to help improve departmental performance in this area.
- **Commercial Skills Shortage:** Several Government Procurement Service (GPS) initiatives have been designed to improve procurement capability and capacity in Government, including a Government Procurement Graduate Scheme (GPGS), Fast Stream Placements and the recently completed GPS Reward Strategy.
- **Lack of Formal Supplier Relationship Management:** OGC is tackling this issue by facilitating the sharing of best practice in Government and taking the lead in promoting its Common Assessment Framework (CAF 360), Public Sector Construction Clients' Forum (PSCCF) and Consultancy Value Programme all of which are designed to encourage the adoption of common approaches when dealing with suppliers to Government.
- **Influencing Spend beyond Core Department:** OGC is facilitating sharing of good practice via its Procurement Capability Reviews and it is developing guidance on the "key levers" available to Departments for influencing outcomes in the wider family organisation networks ie NDPBs, Agencies, etc.

- Commercial Strategy & Business Alignment: OGC has developed and published a Common Commercial Strategy Template that provides advice on the content of an ideal commercial strategy for a public organisation and highlights the need for this document to not only be aligned with the key strategic objectives of each department but also with the wider government policy such as, sustainable procurement.
- Performance Measurement: OGC is encouraging sharing of good practice and developing collaborative procurement. It is also developing a toolkit of performance indicators used in Government and elsewhere that procurement professionals can call on to help control the delivery of good procurement performance.
- Contract Management Skills and Resources: OGC has developed GPS training initiatives in these areas and is working with the National School of Government to revise the Certificate of Competence to be more relevant to departmental needs.
- Need for more Knowledge Management & Sharing: OGC has established several GPS Special Interest Groups and improved access to procurement information on the OGC website, such as revising its Policy and Standards Framework to make it more accessible to users.

#### MAJOR PROJECTS PORTFOLIO REPORT

In 2007–08 a new joint OGC/Cabinet Office initiative, Major Projects Portfolio (MPP) quarterly reporting, was set up which provides reliable and timely reporting on the Government's 40-50 major projects. It is the key vehicle for Government's assessment of the health of the portfolio of major projects, and provides transparency on project performance against common definitions, identifies key issues, and prompts corrective actions.

The first report was produced in March 2008. The report is issued to relevant Permanent Secretaries and Ministers.

To date the MPP reports have indicated that one of the key issues for major projects is recruiting and retaining people with the right level of skills and capability. The turnover rate of Senior Responsible Owners (SROs) is also an issue.

To help address this, OGC is raising the profile of the Project and Programme (PPM) profession by working closely with departments to promote professional standards, best practice and guidance to enhance skills' levels. OGC has a dedicated team driving the PPM profession agenda forward.

#### MAJOR PROJECTS REVIEW GROUP (MPRG)

MPRG is a scrutiny panel for major central government projects, sponsored by HM Treasury. Its aim is to deliver better value for the taxpayer by challenging projects on deliverability, affordability and value for money.

HMT/OGC has considered the emerging themes which have been drawn out from the first year of MPRG reviews and are looking at ways in which to take these forward. The emerging themes are:

##### (a) Commercial Skills

This has been a combination of projects having insufficient commercial expertise and projects having commercial support, but that support being either only part time or of insufficient experience to fully support major procurement projects such as these.

##### (b) Inadequate Governance and Stakeholder management

In some cases this related to a lack of external challenge to the project or to inadequate involvement by the parent department in governance of a project managed by an agency.

##### (c) Inexperienced Senior Responsible Owner (SRO)

Some of the projects reviewed had an SRO who was highly respected in the policy arena and had successfully delivered the policy development stages of the project, but who had no experience of project or programme management. In these cases the level of experienced project management support being provided by others was not high enough.

(d) Isolation from department

This has shown itself in projects not drawing as much as they could on specialist expertise (eg legal and commercial) which is available in the departments and in projects not taking adequate account of the time required for departmental decision making and issue resolution processes.

BEST PRACTICE TOOLS

OGC regularly updates its best practice tools ie Prince 2, Managing Successful Programmes etc.

OGC GATEWAY™ Process

The Gateway Process encourages discussion with SROs about lessons learned from past reviews. Review Team Leaders have experience of reviewing many projects (sometimes up to 50) and always bring the lessons learned from these into discussions with the relevant SRO.

LESSONS LEARNED

OGC has introduced a series of Lessons Learned bulletins—primarily through evidence gathered from OGC Gateway reviews. The first bulletin on “Lessons from Shared Services initiatives” was published on the OGC website in October 2008.

OGC have undertaken in the region of 21 Gateway Reviews to date on Shared Services programmes and projects. The scope of the programmes and projects typically includes an integrated solution for a range of corporate services; covering HR, finance and payroll, estates, IT and procurement. The main lessons which emerge from these Reviews are:

- Develop a sound business case to support the decision and keep this under regular review;
- Have a realistic Benefits Realisation Plan with unequivocal buy-in from the stakeholders;
- Ensure the organisation has the capacity, capability and resources to deliver the Shared Services Solution. Time-scales also need to be realistic;
- Ensure stakeholder buy-in is obtained from the outset and sustained throughout the development and implementation of the Shared Services solution;
- Develop Service Level Agreements which are practical and realistic;
- Develop sound Migration and Transition Plans—including data migration and cleansing;
- Anticipate and manage staff sensitivities through effective communication;
- Develop a Contingency Plan as part of the wider risk management strategy.

OGC will shortly be publishing the second bulletin which will be on “Programme and Project Boards”.

17 February 2009

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## 2. Memorandum from Chelgate Limited

Further to my telephone conversation with the Clerk to the committee, I am attaching background information relating to the questions on construction contracts that Austin Mitchell MP asked Nigel Smith, OGC Chief Executive, at the committee meeting on January 14, 2009.

I would like to clarify one point: Austin Mitchell started his question by saying that his questions were as a result of a call from a member of the public. This is not quite accurate—although my briefing to the Clerk was by telephone, I was not calling as a member of the public. I had, in fact, been trying to contact various members of the committee that morning, both by telephone and email, and had said that I was calling from Chelgate on behalf of the Joint Contracts Tribunal. The final conversation, with the Clerk, a few minutes before the meeting started, was as a result of several calls to the Committee Chairman’s office. I wouldn’t want there to be any misunderstandings.

Michael E Hardware  
Executive Vice President  
Chelgate Limited

16 January 2009

## INTRODUCTION

All significant construction projects in the UK have a written contract. Although some have bespoke contracts drafted specifically for the project, most use a standard form of contract. There are various standard contracts available from three main authoring bodies: The Association of Consulting Architects (ACA), the New Engineering Contract (NEC) and The Joint Contracts Tribunal (JCT).

## HISTORY

Austin Mitchell MP stated in the committee of January 14: “in 2005 OGC decided there should only be one construction contract, limiting Whitehall in construction contracts to one supplier.”

The OGC conducted its original review in 2005 evaluating construction contracts against its *Achieving Excellence in Construction* (AEC) criteria. The review was poorly conducted and implemented to such a degree that the contract authoring bodies were not made aware of the objective, and so did not engage in any great detail in the process. The OGC announced that just one contract, NEC3, met its AEC criteria, and consequently endorsed the use of this form of contract on all public building projects, including the 2012 Olympics. It also provided support and training in the use of NEC contracts.

The other two contract authoring bodies voiced their reservations over the OGC’s actions, but it raises the question whether it is the OGC’s role to favour one supplier of services to government over another?

## REVIEW

Austin Mitchell MP went on to say: “Under pressure, you commissioned a review by Arups, this had recommended that there be three construction contracts not just one, but the OGC are still sitting on the report and apparently want to stick to the one contract, which again would be a cosy relationship.”

JCT and the ACA both independently asked OGC to reconsider its findings, and in 2008 Arup was commissioned by OGC to undertake a review, which reported at the end of September. It found that the Joint Contracts Tribunal (JCT) *Constructing Excellence* contract (JCT-CE) and the Association of Consulting Architects (ACA) *Project Partnering Contract* (PPC2000) both met the criteria, as well as the New Engineering Contract (NEC) *Engineering and Construction* contract (NEC3).

The Arup review said: “Each contract reviewed satisfies OGC’s Evaluation Criteria. Each contract reviewed would enable parties, using them correctly, to achieve OGC’s Achieving Excellence in Construction standards from which the Evaluation Criteria are derived.”

It continued: “No single contract is superior to the other two in all respects—each has its own strengths and weaknesses and each is highly adaptable. The difference in the way that each contract is applied by users will be at least as significant as the differences in the processes or terms and conditions provided within the contract.”

The review has, to date, not been published.

JCT and ACA were advised that the recommendations of the review eg that all three forms of contract met the OGC’s requirements and that this was to be presented to the Public Sector Construction Clients Forum (PSCCF) on December 11. Subsequently, it is understood that this committee was in fact advised by OGC to continue with one contract. Until the review is published so that construction industry interest can see the results of Arup’s work, it is difficult for any of the contract providers to understand OGC’s position. JCT and ACA have been advised by OGC that it wishes to continue with the status quo—to continue the sole endorsement of the use of NEC in public building projects—which brings into question the reason why the review, estimated to have cost £50k, was commissioned if OGC was going to ignore its findings.

Sir Michael Latham, the author of the Government’s original review of the construction industry, has commented on the review: “The construction industry has taken huge strides forward in recent years, but it is still not enough. The OGC has attempted to direct public procurement along the right path to collaborative working, and I am pleased that three contract forms now meet its principles for achieving construction excellence. The widespread adoption of these contracts in the public sector, and hopefully the private sector, will enable the industry to take further steps along the path to best contractual practice.”